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UNCLAS SECTION 01 OF 03 DUBAI 000271

SIPDIS

E.O. 12958: N/A
TAGS: PREL IR ECON
SUBJECT: IRAN'S MAJLIS VOTES TO FREEZE KEY PRICES

¶1. (U) Sensitive But Unclassified - Protect Accordingly

¶2. (SBU) SUMMARY: On January 11 the Iranian Majlis passed a bill fixing the price of gasoline and other key goods and services at September 2004 levels for the upcoming Iranian year 1384 (i.e. March 21, 2005 - March 20, 2006). The bill's proponents say that fixing will decrease inflation and force the government to economize. Opponents label the bill as a political gambit to keep key consumer prices low before the June 2005 Presidential election, a perception which seems to be prevalent among political observers. The Guardian Council is expected to approve the bill. END SUMMARY.

¶3. (U) On January 11 the Iranian Majlis passed a bill fixing the price of key goods and services for the upcoming Iranian year 1384 (March 21, 2005-March 20, 2006) at September 2004 levels. The bill was titled "Substituting Article Three of the Fourth Development Plan (FYDP)," and was more popularly known as the "Stabilizing Goods and Services Bill" (NOTE: Iran's Third FYDP ends March 20, 2005, with the Fourth FYDP starting on March 21, 2005). The Guardian Council is expected to approve the bill.

¶4. (U) This bill revised Article Three of the Fourth FYDP such that the sales price of gasoline, diesel, kerosene, furnace oil and other oil products, as well as gas, electricity, water and drainage service charges, phone call and postal rates in the Iranian year starting March 21, 2005 will remain at Shahrivar month 1383 (i.e. August-September 2004) levels. The bill also stipulates that for the subsequent years of the Fourth FYDP, prices will be set on the basis of plans presented to the Majlis by the government each September, with any suggested price increases for each item having to be justified on socio-economic grounds.

¶5. (U) The bill also mandates that by the end of the second year of the Fourth FYDP (March 20, 2007) the government is obliged to

take sufficient steps, to include economizing in fuel product usage and increasing public transportation capacity, such that all of Iran's domestic needs for fuel products are met by the output of Iran's refineries. The bill also authorizes state-run gas and electricity companies to fine non-industrial entities exceeding the consumption level authorized by the Majlis each year.

ADMINISTRATION ATTACKS PLAN...

¶6. (U) This bill, put forward by the dominant conservative faction within the Majlis, had become a source of much political controversy in the recent weeks. Administration reformists involved in the drafting of the Fourth FYDP, to include Economy and Finance Minister Safdar Hoseyni and Management and Planning Organization (MPO) head Hamid Reza Baradaran-e Shoraka, came out strongly against its passage. MPO head Baradaran-e Shoraka told press that the bill's passage would worsen the existing projected budget deficit. He added that price stabilization in the coming year would obstruct many planned government programs, and that, if the Majlis bill were approved, "the government will have no alternative but to take money from the foreign exchange reserve." President Khatami's Parliamentary Deputy Hojjatoleslam Majid Ansari told press that the bill was contrary to the macro-policies of the Supreme Leader as articulated in the Fourth FYDP, which include creating jobs and optimizing fuel consumption.

¶7. (U) Government spokesman Abdollah Ramazanzadeh told ISNA that the bill had been drafted "based on political objectives." In his December 27, 2004 weekly press conference, Ramazanzadeh spoke out harshly against the (then) draft bill, saying that with the decreased government income, the government would no longer be able to achieve the following goals:

- providing funds for the Social Security system for the poor;

- increasing the resistance of urban and rural buildings and residences to earthquakes;

- expanding and increasing the efficiency of urban and inter-city public transportation, producing duel-fuel automobiles and expanding the supply of compressed natural gas at subsidized prices;

- decreasing the number of incident-prone road locations and equipping a network of emergency pre-hospital and hospital medical care;

- implementing plans to optimize fuel-use technology in factories while decreasing air pollution.

¶8. (U) Ramazanzadeh predicted that the decreased income to government companies would decrease the flow of taxes and profits to the government, and push some of these companies into the red. He also claimed that the decrease in government income would increase the budget deficit, which would in turn increase liquidity, exacerbate inflation and necessitate increased withdrawals from the Oil Stabilization Fund.

GAS PRICES TOO LOW

¶9. (U) Majlis representative Hassan Afarideh, a staunch opponent of the bill, told press before the bill's passage that by keeping gasoline prices artificially low, this bill would have major adverse consequences (the current price is approximately 10 cents/liter, or 40 cents a gallon). He said that Iran was currently using 63 million liters of gasoline daily, with a ten percent annual growth in recent years. If Iran's gasoline consumption continues to grow at the present rate, Iran's daily consumption would be 310 million liters in Iranian year 1400 (March 21, 2021-March 20, 2022). To be produced domestically, this amount would require 6 million barrels of crude oil per day (bpd) for refining, and 40 refineries, the construction of which would cost approximately 80 billion dollars. He said that Iran, with a population of approximately 70 million, was using the same amount of gasoline annually as was India, with a population of over one billion. Afarideh said that low gasoline prices

encourage consumption and decrease economic incentives for getting rid of fuel-inefficient vehicles and bringing to market fuel-efficient vehicles. He urged that instead of fixing Iran's gasoline prices at an artificially low level, the price be raised to the FOB Persian Gulf price.

ON THE OTHER HAND...

¶10. (U) The Majlis Research Center, headed by Tehran representative (and possible Presidential candidate) Ahmad Tavakoli, was the original drafter of the Price Stabilization bill. Tavakoli, known for his pro-statist, anti-free market economic views, has also been one of the bill's main proponents in the Majlis. Contrary to Administration positions, he trumpeted the bill as a major tool in reining in runaway government expenses and controlling inflation. He told press that had the Fourth FYDP been implemented without changing Article 3, it would have caused a severe budget deficit and "rampant inflation that would have dealt a heavy blow to the productive private sector and to exporters." He boasted to press that the price stabilization bill would prevent "back-breaking pressure" on Iran's people and on its private sector producers and manufacturers, and would also prevent both an increase of government presence in the economy and a budget deficit.

¶11. (U) In response to reporters' questions as to whether this bill would decrease government income, Tavakoli explained that the government budget had two parts: the government's general budget and the budget for government companies, banks and subordinate institutions. When Government companies producing goods are not allowed to raise prices, it doesn't affect the government's income but rather only decreases the government's general expenses, as the government itself is a consumer of some of these goods. He claimed that decreased government expenses from buying many goods at last year's rates would partially offset decreased revenue. He also claimed that government companies could compensate for lost revenues by economizing in current expenses (critics have pointed out however that economizing is hard when, for example, existing Iranian labor laws prevent government workers from being dismissed).

¶12. (U) When accused of politicking, Majlis Speaker Gholamali Haddad-Adel replied that since the bill benefited the people, the Majlis should not avoid approving it solely because its passage would be to the political benefit of its supporters. He told Iranian press before the bill's passage that the annual government price increase for these targeted goods and services had created many problems for the people, especially fixed-wage earners and the poor. He claimed that the government should think of 'other ways' to overcome economic problems, besides raising prices. He told press that this bill's passage was just one step in the Majlis's ongoing efforts to combat "financial indiscipline."

¶13. (SBU) COMMENT: Based on anecdotal information gleaned by Poloff, the popular perception among political analysts is that the Majlis's motivation in passing the bill passage was in fact exclusively political, to bolster the conservatives' popularity before the June 2005 Presidential election. The consensus of Iran's economists as reflected in Iranian print media seems to be that the bill's overall effect will be deleterious, increasing the government's budget deficit and crippling government efforts to decrease gasoline usage by bringing its price in line with regional prices.

¶14. (SBU) COMMENT CONT'D: The passage of this bill, like the Majlis cancellation of the "Tav" and "Turkcell" contracts, the possible cancellation of the Renault L-90 automobile contract, and other similar measures being considered by the Majlis, is another indication that this Majlis's agenda is being set by its so-called 'neo-conservatives,' i.e. the younger, radicalized conservatives aligned with the IRGC and the "Isargaran" political party, as opposed to the traditional conservative faction aligned with the Islamic Coalition Association ('Motalafeh') and the Militant Clergy Association ('Ruhaniat'), who were predominant in the Fourth and Fifth Majlis (1992-96,

1996-2000). This group is pursuing a policy of decreasing the influence of foreign companies on the Iranian economy and increasing state intervention, reversing the general trend of the Khatami years.